



Research Paper

An Examination of the Financing Strategy and Challenges Linked to Capitalization Concerning Manufacturing SMEs in Pune Region of India

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ABSTRACT: This study aimed to grasp and identify the financing approaches utilized by Manufacturing SMEs throughout different phases of their life cycle. The enterprises might need funds for various purposes, and as a result, they may need to obtain financing from various sources. The utilization of various capital structures to reduce the overall cost of capital depends upon the size of the enterprise and the available sources of finance. This study identified and analysed the variations in the various aspects of financing strategy. Hence, the present study identified and analysed the significant challenges linked to capitalization and the experiences related to securing finance from various lending institutions. To support SMEs, the government is making substantial efforts by offering various schemes. The study aimed to analyse the awareness of the chosen government schemes.

The present study employed a descriptive research design. Data on the perceptions of respondents from Manufacturing SMEs were gathered through primary source using a structured questionnaire. Primary data was gathered from 385 registered Manufacturing small and medium enterprises using a random sampling method. Secondary data, including published literature, previous research, and government and non-government publications, were utilized to establish a robust foundation for this study. The study employed Chi-Square test, One-way ANOVA, and Two-way ANOVA to test the hypothesis.

The outcome of the study reveals 'Financing Strategies' embraced by Manufacturing Small and Medium Enterprises at different stages of their lifecycle. The study also shows that Manufacturing Small and Medium Enterprises may opt for different financial strategies based on their life stages.

Key Words: SME, Financing strategy, Capitalization, Lifecycle, ANOVA, Chi-Square etc.

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I. INTRODUCTION

The present study aims to analyse the various funding options accessible to business entities to enhance understanding and decision-making regarding financial resources. Exploring the available funding choices for business entities is crucial for understanding the financial landscape and optimizing resource acquisition. This study seeks to explore and identify the specific approaches employed by SMEs to secure financing, providing insights into effective financial strategies for small and medium-sized enterprises.

The progress and development of every business organization are significantly influenced by the pivotal role of finance. Strategically handling finances is vital in the dynamically evolving landscape of the diverse business environment. The study seeks to understand the various 'Financing Strategies' implemented by Manufacturing Small and Medium Enterprises (SMEs) based on their life stages. These are identified as the Start-up stage, Survival stage, Growth stage, and Sustainment stage.

Over the years, the Small and Medium Enterprises (SME) sector within the Ministry of Micro, Small, and Medium Enterprises (MSME) has evolved into a remarkably lively and dynamic component of the Indian economy. The sector plays a substantial role in advancing the socio-economic progress of the country by promoting entrepreneurship and providing the most substantial employment opportunities, ranking second only to the Agricultural sector.

The research objective is to examine and address the challenges encountered by SMEs during the capitalization process, contributing to the development of strategies for overcoming financial obstacles in the business sector. This study seeks to evaluate the ways in which different government schemes contribute to the

advancement of SMEs, providing valuable insights into the impact of public policies on the growth and sustainability of these enterprises.

Various aspects of 'Financing Strategy and Challenges Related to Capitalization' were discerned through the research gap. These include Objectives of financing, Preferred sources of finance, Preferred financing strategy/capital composition, Ratings based on experience with lending institutions, Various challenges encountered, and Awareness of diverse government schemes.

II. LITERATURE REVIEW

Nguyen, B. (2020) explores the connection between corporate investment and the chosen financing strategy. The research involved hypothetical examination in which investigators explored the correlation among four distinct funding strategies which includes no external finance, informal finance exclusively, both formal and informal finance, and formal finance solely. The main dependent variable examined was firm investment, with independent variables including funding sources, social networks, gender, age, business age, firm size, export, innovation, affiliation, and liability, employed for hypothesis testing. The examination of the results included the application of regression analysis and coefficients of association for testing purposes. The research revealed that businesses utilizing external financing engage in notably higher levels of investment compared to those that do not employ such financing.

Ayodotun Stephen Ibidunni (2018) examined the Financing Strategy, entrepreneurial skills, and business expansion of SMEs in Nigeria. The study incorporated demographic variables (Gender, Marital status, Age bracket, Educational qualification), independent variables (Personal savings, Bank loan, Venture capital, Business Donations, Skills, Attitude, Knowledge), and dependent variables (Profit growth, Sales growth, and Employee growth). The researcher used a standardized survey for collecting data and applied descriptive statistics and multiple regression for analysis. The findings indicated a significant influence of venture funding and corporate donations on the profit growth of technology-based Small and Medium-sized Enterprises (SMEs).

Gheribi, Sara & Klemens, Anita & Klepacz, Maria & Kotnicka, Agata. (2018) have emphasised on identifying potential sources of financing for start-up companies. The researchers discovered that start-up companies showed a preference for utilizing internal funds as a means of raising capital, in addition to considering options such as public funds, venture capital, business angels, and accelerator programs. The researchers identified various funding sources, among which were bank loans.

H. Kent Baker, Satish Kumar, Purnima Rao (2017) have explored the financing choices and approaches adopted by SMEs in India, with an emphasis on SMEs located in the north-western region of the country. The report explores six primary research domains specifically pertaining to SMEs. They include types of internal and external sources of funding employed by Indian SMEs; SMEs' preference for financing sources like short, medium, and long-term; internal and external sources of financing were rated based on SMEs' opinions., The factors which influence SMEs' financing preferences and practice, and the consistency of SMEs' financing decisions. Data was collected from 309 small businesses to investigate the array of financing alternatives available to them. The study's findings indicated that the respondents expressed a choice for internal funds, subsequent to long-term loans, and funds from government and financial institutions.

Junpeng Wang, Liai Lun Chen (2016) have conducted a study to pinpoint practical policy measures that high-tech enterprises can implement to address their financial challenges. The study proposed that enterprises could adopt an innovative financing approach by securing funding from suppliers, vendors, and other affiliated parties.

Sonia Baños-Caballero, (2015) have found that the success of a company was influenced by its working capital financing approach. The researchers affirmed that adopting a working capital requirement (WCR) financing strategy aids enterprises in enhancing their performance. It was mentioned that the ownership structure leads to variations in the financing strategy among different types of enterprises.

According to Kapoor, Amitesh (2012), there existed a variety of funding sources; however, SMEs showed a choice for informal financing sources. The researcher recommended that SMEs should contemplate all available finance sources.

III. RESEARCH GAPS

1. The primary difference from prior studies is found in the geographical area. This research specifically focuses on Manufacturing SMEs in the Pune Region within the state of Maharashtra, India.
2. The difference in sample size is evident, with a previous study utilizing a sample size of less than one hundred.
3. It is noted that a significant portion of the studies relies on secondary data to explore the diverse financing sources employed by SMEs, as well as the associated challenges in raising funds as part of their financing strategy.

4. There is need felt to emphasized the importance of examining the decisions made by SMEs concerning various financing sources and the strategies they utilize for securing funds Key factors that impact business decisions when choosing the right finance source and adopting suitable financing strategies involve significant challenges in obtaining necessary funds and awareness of various government schemes. Therefore, it is crucial to analyse the different challenges and levels of awareness regarding government schemes among SMEs at various phases of their life cycle.

5. Examining the preferences expressed by SMEs regarding different finance sources and their financing strategies is essential. The influential factors affecting enterprise decisions in choosing the right finance source and adopting appropriate financing strategies include significant challenges in obtaining necessary funds and awareness of diverse government schemes. Hence, it is crucial to analyse the varied challenges and awareness levels of government schemes among SMEs at different stages of their life cycle.

IV. RESEARCH PROBLEM

Securing appropriate and sufficient financing poses a challenging task for businesses. Adopting a methodical approach to choosing diverse financing sources contributes to the sustainable growth of enterprises. The present study tries to examine and identify the specific approaches employed by Small and Medium Enterprises (SMEs) to obtain financing, aiming to provide a comprehensive understanding of the strategies utilized by SMEs in obtaining financial resources for their operations and growth. The research problem involves examining and assessing the ways in which various government schemes contribute to the advancement of Small and Medium Enterprises (SMEs). This investigation seeks to understand the impact and effectiveness of government initiatives on the progress and advancement of SMEs.

V. RESEARCH QUESTIONS

- 1) What are the primary financial resources utilized by SMEs throughout their different stages of development?
- 2) What are the various financing strategies utilized by SMEs?
- 3) What challenges do Small and Medium Enterprises encounter throughout their life stages in fulfilling their financial needs?
- 4) How do Small and Medium Enterprises perceive their experiences with different lending institutions?
- 5) Are Small and Medium Enterprises knowledgeable about the various schemes offered by the Government?

VI. OBJECTIVES OF THE STUDY

- 1) To examine the primary financial resources employed by SMEs across their various stages of development.
- 2) To identify the diverse financing strategies employed by SMEs
- 3) To recognize the different challenges encountered by enterprises throughout their life stages.
- 4) To understand the experience of SMEs when seeking funds from different lending agencies.
- 5) To evaluate the awareness of various government schemes among SMEs.

VII. HYPOTHESIS OF THE STUDY

- 1) The life stage of an enterprise does not show a significant correlation with the diverse sources of finance utilized by SMEs.
- 2) The life stage of enterprises does not exhibit a significant correlation with their financing strategy.
- 3) The life stage of an enterprise does not demonstrate a significant association with the diverse challenges it encounters.
- 4) The difference in experience ratings when seeking funds from various lending institutions is not statistically significant.
- 5) The awareness of various Government Schemes does not vary significantly across different life stages of SMEs.

VIII. RESEARCH METHODOLOGY

The current study employed a descriptive research design. The research relies on the perspectives of Small and Medium Enterprises (SMEs) respondents. This qualitative research involves the collection and analysis of data through the utilization of standardized questionnaires. Additionally, the study integrated information from reports and published literature.

The unit of sampling for this study comprises Small and Medium Enterprises (SMEs) in the Pune Region engaged in manufacturing. There were a total of 12,116+ registered Small and Medium Enterprises (SMEs) in the Pune Region engaged in manufacturing. According to the Krejcie & Morgan Table, a sample size

of 378 is needed for a population of 25,000 with a confidence level of 95%. However, to enhance result precision, a sample size of 385 was chosen for the study. Samples were chosen appropriately through the utilization of a simple random sampling method.

The study relies on the primary data gathered through individual discussions/meetings, and a survey was carried out by distributing standardized questionnaires to the respondents. A questionnaire was completed by 400 respondents, but 15 were excluded from the survey due to ambiguity. As a result, the study employed data from 385 respondents. Further, the secondary data was obtained from published sources, including MSME annual reports, and survey reports etc.

The assessment of internal consistency involved by applying the Cronbach's Alpha test, while the normality was examined through the Kolmogorov-Smirnov test. The relationship among variables was explored using the Chi-square test, One-way ANOVA, and Two-way ANOVA test.

IX. VARIABLES OF THE STUDY

The study included both dependent and independent variables. The dependent variables covered sources of finance, financing strategy, challenges, experience with lending institutes, and awareness of government schemes. The independent variable is the life stage.

X. ANALYSIS & RESULTS

This research employs distinct phases of enterprise development to evaluate the diverse financial approaches employed by SMEs at various points in their life cycle. The study categorized the life stages as follows:

- i) Initial phase (Under 3 years),
- ii) Establishment phase (3 to 6 years),
- iii) Expansion phase (6 to 10 years), and
- iv) Maintenance phase (exceeding 10 years)

Table 1: Categorization of SMEs based on the developmental stage of the business

Sr. No.	Stages	Frequency	Percentage (%)
1	Initial phase (Under 3 years)	92	23.90
2	Establishment phase (3 to 6 years)	99	25.71
3	Expansion phase (6 to 10 years)	67	17.40%
4	Maintenance phase (exceeding 10 years)	127	32.99%
	Total	385	100%

(Source: Primary data)

Table 2: Legal standing of the enterprises

Sr. No.	Stages	Frequency	Percentage (%)
1	Sole ownership	172	44.68
2	Partnership	72	18.70
3	Privately held limited company	129	33.51%
4	Others	12	3.11%
	Total	385	100%

(Source: Primary data)

Table 3: Objectives of Obtaining Funding

Sr. No.	Objectives	Frequency	Percentage (%)
1	Finance for Operational Capital	129	33.51%
2	Secured Loan Financing	33	8.57%
3	Overdraft	24	33.51%
4	Long-term finance	188	48.83%
5	Any other alternative option	11	2.86%
	Total	385	100%

(Source: Primary data)

Table 4: Sources Fund Preferred by SMEs

Sr. No.	Sources of Fund	Frequency	Percentage (%)
1	Own Capital/ Personal fund	63	16.36%
2	Loans from Family/Relatives	39	10.13%
3	Borrowings from banks/ financial institutions	162	42.08%
4	Government aid	121	31.43%
	Total	385	100%

(Source: Primary data)

Table 5: Funding Strategies/Approaches Preferred by SMEs

Sr. No.	Funding Strategies/Approaches	Frequency	Percentage (%)
1	Ownership Capital only	43	11.17
2	Debt/Loan only	34	8.82%
3	Equity>Debt	170	44.16
4	Equity = Debt	53	13.77
5	Equity < Debt	85	22.08
	Total	385	100

(Source: Primary data)

Table 6: Major Challenges encountered by SMEs

Sr. No.	Major Challenges	Frequency	Percentage (%)
1	High interest on Loan	87	22.59
2	Challenges with providing collateral	132	34.28
3	Insufficient awareness of existing schemes	53	13.76
4	High Loan Processing charges	51	13.24
5	Extended duration for processing the loan application	27	7.01
6	Challenges in obtaining or finalizing the necessary paperwork	35	9.09
	Total	385	100%

(Source: Primary data)

Table 7: Ratings based on the track record/Experience Ratings of Lending Institutions

Lending Institutions	Extremely Poor		Poor		Neutral		Good		Excellent		Total	
	Count	%	Count	%	Count	%	Count	%	Count	%	Count	%
Nationalized Bank	86	22.34	113	29.35	68	17.66	98	25.45	20	5.19%	385	100
Private Bank	59	15.32	78	20.26	72	18.70	110	28.57	66	17.14	385	100
Co-operative Bank	58	15.06	100	25.97	78	20.26	97	25.19	52	13.51	385	100
Non-Banking Financial Company (NBFC)	59	15.32	78	20.26	69	17.92	113	29.35	66	17.14	385	100
Borrowings from friends/ relatives	82	21.30	96	24.94	63	16.36	72	18.70	72	18.70	385	100
Any other	86	22.34	139	36.10	65	16.88	75	19.48	20	5.19	385	100

(Source: Primary Data)

Hypothesis Testing Results:

1) H_0 : The life stage of an enterprise does not show a significant correlation with the diverse sources of finance utilized by SMEs.

H_1 : The life stage of an enterprise shows a significant correlation with the diverse sources of finance utilized by SMEs.

	Value	df	Asymp.Sig (2-sided)
Pearson Chi-Square	33.692 ^a	9	.000
Likelihood Ratio	34.805	9	.000
Linear-by-Linear Association	2.411	1	.120
N of Valid Cases	385		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 6.79.

(SPSS Output)

Chi Square (χ^2) Calculated Value	Chi Square (χ^2) table value (df = 9, α = 5%)	Decision
33.692	16.92	H ₀ Rejected

(SPSS Output)

Inference: The calculated Chi-square (χ^2) value is 33.692, surpassing the Chi-square (χ^2) table value of 16.92 for 9 degrees of freedom (d.f.) and a 5% level of significance (α). Consequently, the null hypothesis (H₀) is not accepted. Therefore, the conclusion is that the life stage of an enterprise shows a significant correlation with the diverse sources of finance utilized by SMEs.

2) H₀: The life stage of enterprises does not exhibit a significant correlation with their financing strategy

H₁: The life stage of enterprises exhibits a significant correlation with their financing strategy

	Value	df	Asymp.Sig (2-sided)
Pearson Chi-Square	38.659 ^a	12	.000
Likelihood Ratio	37.455	12	.000
Linear-by-Linear Association	.019	1	.891
N of Valid Cases	385		

a. 0 cells (.0%) have expected count less than 5. The minimum expected count is 5.92.

(SPSS Output)

Chi Square (χ^2) Calculated Value	Chi Square (χ^2) table value (df = 12, α = 5%)	Decision
38.659	21.03	H ₀ Rejected

(SPSS Output)

Inference: The calculated Chi-Square (χ^2) value is 38.659, exceeding the Chi-Square (χ^2) table value of 21.03 for 12 degrees of freedom (df) and a 5% significance level (α). Hence, the null hypothesis (H₀) is not accepted. Therefore, the life stage of enterprises exhibits a significant correlation with their financing strategy.

- 3) H_0 : The life stage of an enterprise does not demonstrate a significant association with the diverse challenges it encounters.
 H_1 : The life stage of an enterprise demonstrates a significant association with the diverse challenges it encounters.

	Value	df	Asymp.Sig (2-sided)
Pearson Chi-Square	30.004a	15	.012
Likelihood Ratio	30.098	15	.012
Linear-by-Linear Association	.373	1	.541
N of Valid Cases	385		

a. 1 cells (4.2%) have expected count less than 5. The minimum expected count is 4.70.

(SPSS Output)

Chi Square (χ^2) Calculated Value	Chi Square (χ^2) table value (df = 9, α = 5%)	Decision
30.004	25.00	H_0 Rejected

(SPSS Output)

Inference: The computed Chi-Square (χ^2) value of 30.004 exceeds the critical Chi-Square (χ^2) table value of 25.00 at a 5% significance level for 15 degrees of freedom (d.f.). Consequently, the null hypothesis (H_0) is rejected. Therefore, the life stage of an enterprise demonstrates a significant association with the diverse challenges it encounters.

- 4) H_0 : The difference in experience ratings when seeking funds from various lending institutions is not statistically significant.
 H_1 : The difference in experience ratings when seeking funds from various lending institutions is statistically significant.

Table 8: One-Way Anova Result

Sources of Variations	SS	DF	MS	F	P-Value	F. Crit.	Decision
Between Groups	10260.3	4	2565.08	7.89	0.00029	2.76	H_0 Rejected
Within Groups	8123.67	25	324.947				
Total	18384	29					

(SPSS Output)

Inference: As the p-value falls below 0.05, the acquired F ratio, with degrees of freedom (4, 25) equal to 7.89, surpasses the critical F value of 2.76. This leads to the conclusion that the observed F-ratio is probably not a result of random chance at a significance level of $p < 0.05$. Hence, there is a notable variance in the experience ratings associated with seeking funds from different lending institutions. Thus, the null hypothesis (H_0) is rejected. Therefore, the difference in experience ratings when seeking funds from various lending institutions is statistically significant.

- 5) H_0 : The awareness of various Government Schemes does not vary significantly across different life stages of SMEs.
 H_1 : The awareness of various Government Schemes vary significantly across different life stages of SMEs.

Table 9: Two-Way Anova Result

Sources of Variations	SS	DF	MS	F	P-Value	F. Crit.	Decision
Between Groups	4206.72	14	300.48	2.75	0.00365	1.87	H ₀ Rejected
Within Groups	184646.6	4	46161.65				
Error	6107.813	56	109.0681				
Total	194961.1	74					

(SPSS Output)

Inference: Due to the p-value being below 0.05, the calculated F ratio, with degrees of freedom (14, 4) equal to 2.754976, exceeds the critical F value of 1.872588. Consequently, it is inferred that the observed F-ratio is likely not a chance occurrence at a significance level of $p < 0.05$. Hence, there is a noteworthy variation in the awareness of various Government Schemes among SMEs. Thus, the null hypothesis (H_0) is rejected. Therefore, the awareness of various Government Schemes vary significantly across different life stages of SMEs.

XI. FINDINGS OF THE STUDY

- 1) This study indicates that in the Start-up and Survival stages, a majority of enterprises favoured Government Assistance as their primary source of finance, while in the Growth and Sustenance stages, a majority of enterprises leaned towards 'Borrowings from banks/financial institutions.
- 2) In the Start-up, Growth, and Sustenance stages, the majority of enterprises opted for a financing strategy/composition of capital characterized by a higher proportion of equity and a lower proportion of debt (Equity>Debt). Conversely, during the Survival stage, most enterprises favoured a financing strategy/composition of capital with a lower proportion of equity and a higher proportion of debt (Equity<Debt).
- 3) Among the challenges encountered by Manufacturing SMEs, the study indicates that Start-up stage enterprises primarily grapple with the significant challenge of high lending rates, while Survival stage, Growth stage, and Sustenance stage enterprises predominantly face the challenge of difficulties in providing collateral.
- 4) The study examined the experience ratings of different lending institutions in obtaining finance. Enterprises provided ratings on a scale including categories such as Extremely Poor, Poor, Neutral, Good, and Excellent. Private Banks and Non-Banking Financial Institutions (NBFC) received favorable ratings categorized as "Good," while nationalized banks and Cooperative Banks received less favorable ratings categorized as "Poor." Borrowings from friends/relatives and any other sources received the lowest experience ratings classified as "Extremely Poor."

XII. SUGGESTIONS

- 1) Start-up stage manufacturing SMEs might prioritize Government schemes and loans from banks as their preferred sources of finance. Manufacturing SMEs might opt for a financing strategy that emphasizes a higher proportion of equity and a lower proportion of debt (Equity>Debt) to attain their long-term objective(s).
- 2) Survival stage manufacturing SMEs might seek increased support from government schemes as a financing source. Manufacturing SMEs may strategically opt for a financing approach characterized by a lower proportion of equity and a higher proportion of debt (Equity<Debt).
- 3) In the growth stage, manufacturing SMEs might prioritize obtaining funds from banks or financial institutions as a primary source of finance. Manufacturing SMEs may opt for a financing strategy emphasizing a higher proportion of equity and a lower proportion of debt (Equity>Debt) or a strategy that involves more equity and less debt (Equity>Debt) to attain their long-term business objectives.
- 4) During the Sustenance Stage, small and medium-sized manufacturing enterprises may prioritize obtaining funds from banks or financial institutions as a primary source of finance. Manufacturing SMEs may opt for a financing strategy characterized by a higher proportion of equity and a lower proportion of debt (Equity>Debt).
- 5) In the initial start-up and survival stages, manufacturing SMEs actively seek government assistance. Hence, it is imperative for the government to intensify its efforts to enhance awareness of the diverse schemes and proactively engage with SMEs to ensure that the assistance effectively reaches those in need.

XIII. CONCLUSIONS

The investigation indicated that primary funding sources for manufacturing SMEs include loans from banks/financial institutions and government assistance. Manufacturing SMEs favoured a balanced approach of equal equity and debt in their financing strategies. Nevertheless, these enterprises encounter challenges in providing collateral and contend with high lending rates as significant obstacles in raising funds. This indicates that a significant portion of SMEs often encounters challenges in presenting the required security, experiencing difficulties in furnishing the collateral necessary to secure loans.

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